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# Mortgages--Foreclosure--Effect on Junior Liens--Repurchase by Mortgagor Dorff v. Bornstein, 227 N.Y. 236 (1938))

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MORTGAGES—FORECLOSURE—EFFECT ON JUNIOR LIENS—REPURCHASE BY MORTGAGOR.—Defendant purchased real property from the plaintiff and agreed to assume a first mortgage held by the Title Guarantee & Trust Co. Defendant also gave to plaintiff a purchase money mortgage which the parties expressly agreed should be a junior and subordinate lien to the first mortgage. The holder of the first mortgage bid the property in on foreclosure sale and four months thereafter sold it to the children of the defendant. This action is brought to foreclose the second mortgage on the theory that the defendant fraudulently conspired to effect a foreclosure of the first mortgage and that the present owners were dummies acting for him, and by reason thereof plaintiff's lien should become revested. Special Term found that the whole transaction was tainted with fraud and upheld plaintiff's contention. Upon an appeal from an affirmance by the Appellate Division, *held,* reversed. Inasmuch as the income from the property was insufficient to meet the fixed charges, and no affirmative proof of fraud was shown, the finding of fraud and collusion was against the weight of evidence. *Dorff* v. *Bornstein, 277* N. Y. 236, 14 N. E. (2d) 51 (1938).

The modern doctrine [1] is that the mortgagee has no estate in or title to the land; nor has he the right of possession either before or after the mortgage becomes due.[2] He only acquires such title by purchase at the foreclosure sale.[3] The effect of the foreclosure deed is to cut off the mortgagor's equity of redemption [4] and to vest in the purchaser the entire interest and estate of the mortgagor as it existed at the date of the mortgage, unaffected by subsequent encumbrances and conveyances of the mortgagor.[5] The foreclosure being perfect, a new estate in the new owner is created and the rights of subsquent mortgagees are finally and forever extinguished.[6] The purchaser ordinarily having absolute title may do with the land whatever he deems proper and may even convey it to the original owner without thereby

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[1] The modern lien theory, applied in New York, is that the mortgagee has a mere lien on the property, or right to have the specific property sold and the proceeds applied to the payment of the debt. Under strict common law rule, still applied in many states, the mortgage was deemed a conveyance and the mortgagor merely retained an equity of redemption. 1 JONES, MORTGAGES (8th ed. 1928) § 12.

[2] Ten Eyck v. Craig, 62 N. Y. 406 (1875).

[3] N. Y. CIV. PRAC. ACT § 1085: "A conveyance upon a sale made pursuant to final judgment in an action to foreclose a mortgage upon real property vests in the purchaser the same estate only that would have vested in the mortgagee if the equity of redemption had been foreclosed." (The statute refers to the strict common law theory. See note 1, *supra.*)

[4] Lansing v. Goelet, 9 Cow. 345 (N. Y. 1827).

[5] 3 JONES, *op. cit. supra* note 1, §§ 2121, 2122, 1653, 1654; Chicago & Vincennes R. R. v. Fosdick, 106 U. S. 47 (1882); Rector v. Mack, 93 N. Y. 488 (1883); Sautter v. Frick, 229 App. Div. 345, 242 N. Y. Supp. 369 (4th Dept. 1930), *aff'd,* 256 N. Y. 535, 177 N. E. 129 (1931).

[6] Instant case at 241; Hopkins v. Wolley, 81 N. Y. 77 (1880); Plum v. Studebaker Co., 89 Mo. 162, 1 S. W. 217 (1886); Huzzey v. Heffernan, 143 Mass. 232, 9 N. E. 570 (1887).

revesting the subordinate liens.[7] If, however, there is collusion between the original owner and the first mortgagee or if the transaction is tainted with fraud then said owner on repurchase would not take the property free from the subordinate liens.[8] Again the original owner might be estopped from denying the revesting of subordinate liens where the mortgagor inserts unconditional covenants of warranty against incumbrances without expressly excepting the first mortgage;[9] or where he has some duty[10] and fraudulently acts to cut off the interest of the mortgagee by omitting to meet the obligation. Upon repurchase under such circumstances the original owner becomes seized in trust[11] for the subordinate mortgagee.

The New York rule seems to be clearly settled that in the absence of fraud, and of any contract duty or trust towards the junior lienors, a mortgagor may repurchase property from a *bona fide* purchaser and thereby acquire a perfect title. It would seem that the benefit resulting to the mortgagor in such case would be merely incidental to the desire to protect the *bona fide* purchaser in his disposition of the property. The latter buys at the foreclosure sale with the understanding that he is going to be able to give a clear title to *anyone* to whom he sells. Naturally his market is limited if he cannot convey such a title to the mortgagor, who, if he is financially able, would probably be a prospective buyer. Where, however, the original mortgagor bids in the property, the reason for the rule would not exist, and in such case it would appear that the repurchase would inure to the benefit of the junior lienors.[12]

In some states the junior mortgagee may rest his claim upon statutory provisions. A Mississippi court basing its decision on statutes[13] held that the reacquired title of the mortgagor inures to the

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[7] Instant case at 242; Plum v. Studebaker Co., 89 Mo. 162, 1 S. W. 217 (1886), cited *supra* note 6; Federal Farm Mortgage Corp. v. Larson *et al.*, — Wis. —, 278 N. W. 421 (1938).

[8] Mendenhall v. Hall, 134 U. S. 559, 10 Sup. Ct. 616 (1890); Stiger v. Mahone, 24 N. J. Eq. 426 (1874); Tompson v. Heywood, 129 Mass. 401 (1880).

If the income from the mortgaged premises is not sufficient, the mortgagor is not acting fraudulently by omitting to use personal funds to keep the first mortgage from default. Instant case at 240.

[9] Parsons v. Little, 66 N. H. 339, 20 Atl. 958 (1890); Baird v. Chamberlain, 60 N. D. 784, 236 N. W. 724 (1931). Accord: Ayer v. Philadelphia and Boston Face Brick Co., 157 Mass. 57, 31 N. E. 717 (1892) (a statement in the granting clause to the effect that there is a prior mortgage will not save the mortgagor from being estopped when he reacquires title).

[10] Oliphant v. Burns, 146 N. Y. 218, 40 N. E. 980 (1895); Pines v. Novick, 168 App. Div. 155, 153 N. Y. Supp. 891 (2d Dept. 1915) (where mortgagor had to pay taxes and assessments and keep the mortgaged premises free from the paramount governmental lien).

[11] National Surety Co. v. Walker, 148 Iowa 157, 125 N. W. 338 (1910); Wheeler v. Hardy, 123 Misc. 775, 206 N. Y. Supp. 148 (1924); 3 JONES, *op. cit. supra* note 5, § 841.

[12] 3 JONES, *op. cit. supra* note 5, § 2429.

[13] MISS. CODE ANN. (1930) §§ 2124, 2125; applied in Martin v. Raleigh,

benefit of the second mortgagee. California [14] and North Dakota [15] have enacted similar legislation.

J. Z.

MORTGAGES—REAL—PERSONAL — "AFTER-ACQUIRED" CLAUSE. —The plaintiff is the holder by mesne assignments of a first mortgage. The defendant is the purchaser of the furnishings of the hotel which were sold under a chattel mortgage when the owner went into bankruptcy. The plaintiff instituted proceedings to foreclose the realty mortgage and claimed that the furniture, furnishings, kitchen equipment and other contents of the building were subject to the mortgage by virtue of a clause contained therein which, after describing the real property in detail, contained the following clause of coverage: "together with all fixtures and articles of personal property, now or hereafter attached to, or used in connection with the premises, all of which are covered by this mortgage." [1] The building loan mortgage provided that the loan should be advanced from time to time as the building progressed. When the final payment was made there was an outstanding conditional sales contract on file embracing furniture. Subsequently, a chattel mortgage upon the furnishings and movables was executed and delivered by the owner. On appeal from a judgment for plaintiff, *held,* reversed. The facts and circumstances with respect to the personal property in controversy do not justify a conclusion that it was included within the terms of the mortgage. *Manufacturers Trust Company* v. *Peck-Schwartz Realty Corporation,* et al., 277 N. Y. 283, 14 N. E. (2d) 70 (1938).

The movables in the instant case would come within the terms of the coverage clause: (1) if they became fixtures [2] as a matter of

146 Miss. 1, 111 So. 448 (1927) (the mortgagor repurchased foreclosed property from the grantee of buyer at foreclosure sale).

[14] CAL. CIV. CODE (Deering, 1937) § 2930.

[15] N. D. COMP. LAWS (1913–25) § 6731. Both California (see note 14, *supra*) and North Dakota have enacted that "title acquired by the mortgagor subsequent to the execution of the mortgage inures to the mortgagee as security for the debt in like manner as if acquired before the execution." It has been interpreted to apply to cases where the mortgagor had title, lost it, and subsequently reacquired title, as much as to cases where the mortgagor not having title at first acquired it subsequent to the mortgage. Jensen v. Duke, 71 Cal. App. 210, 234 Pac. 876 (1925); Merchants National Bank of Fargo v. Miller, 59 N. D. 273, 229 N. W. 357 (1930).

[1] This is the same clause as the one read into a mortgage by statute except that the words "now or hereafter" and "all of which are covered by this mortgage" are not included in the statutory form. N. Y. REAL PROP. LAW § 254, subd. 1, Cons. Laws, c. 50.

[2] Ford v. Cobb, 20 N. Y. 344 (1859). A fixture is a thing permanent in its nature which has lost the character of personal property and has become a part of a definite parcel of land by permanent annexation. Whether the thing has